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ABSTRACT

This background paper was developed for the Community Services Administration (CSA) in order to provide background information concerning welfare reform. It examines possible public assistance strategies, such as the following: (1) broad-based cash transfer (negative income tax, wage rate subsidies, demogrants, and family allowances), (2) categorical cash transfers, (3) in-kind (consumption) transfers (food stamps), and (4) composite programs. The paper also discusses various normative, economic, social, administrative, and political issues raised by the welfare reform controversy. One issue discussed at length, is that of work incentives and their importance, especially in terms of their relevance in the redesign of America's public assistance system. The potential role of the Community Services Administration in welfare reform is also analyzed. A selective bibliography on welfare reform is included. (Author/AM)

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A REVIEW OF THE MAJOR ISSUES
AND PROBLEMS OF
WELFARE REFORM

A Background Paper
Developed for the
Community Services Administration

February 3, 1977

CSA grant #30161-G-76-01

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U.S. DEPARTMENT OF HEALTH,
EDUCATION & WELFARE
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WELFARE REFORM ANALYSIS

1.0 BACKGROUND AND PURPOSE

On January 24, 1977, Secretary of DHEW Joseph Califano announced the undertaking of a thorough review of the "welfare reform" issue. A report and recommendations will be presented to the President in May 1977. A need, therefore, exists for timely analysis and recommendations by CSA in the forthcoming policy discussions.

This report is designed to provide CSA with brief background information concerning welfare reform. Following an examination of possible public assistance strategies, TARP will discuss major issues facing policymakers in the selection of an appropriate alternative. In the final section of this report, CSA's potential role in welfare reform will be scrutinized.

A review of welfare reform proposals and issues will accomplish several purposes:

1. Acquaint CSA staff with major economic, political, and social policy issues surrounding the debate over welfare reform. Each alternative approach will be critically examined.
2. Focus on those topics and issues which CSA might consider as part of this mandate. TARP will examine CSA's possible role in a new welfare system.
3. Link the Market Basket Study to the specific aspects of welfare reform where there are manifest linkages.

2.0 ALTERNATIVE STRATEGIES FOR WELFARE REFORM

2.1 Overview of Policies Designed to Alleviate Poverty

The United States has relied upon an extensive number of policies designed to alleviate economic deprivation, whether temporary or chronic. Exhibit I presents an enumeration of such actual or potential measures. Given the scope of this report, a detailed analysis of all options is not possible; instead, attention will be concentrated on those specific income redistribution strategies referred to as "direct assistance":

1. Cash Transfer

a. Broad-Based

- i. Negative Income Tax (NIT)
- ii. Wage Rate Subsidies (WRS)
- iii. Family Allowances
- iv. Demogrant

b. Categorical Cash Transfers, e.g., AFDC

2. In-Kind Transfers

a. Consumption, e.g., food stamps, housing, medication

3. Composite: Attempts to combine various direct assistance measures in an integrated, composite whole

2.2 Broad-Based Cash Transfers

2.2.1 Negative Income Tax (NIT)

The negative income tax (NIT) is a broad-based cash transfer program which adjusts the amount of the transfers according to family income and size. In other words, for a family of a given size, the lower the income, the larger the transfer.

Three policy variables concisely describe a program of this type:

- income guarantee: the amount transferred to a family with zero income
- marginal tax rate: the proportion or rate of reduction of the transfer as a family's pre-transfer income rises

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EXHIBIT I: National Income Transfer Programs*

I. Direct Assistance

A. Cash Transfers

1. Broad-Based
 - a. Negative income tax
 - b. Wage rate subsidies
 - c. Family allowance
 - d. Demogrants
 - e. Old Age, Survivors, and Dependents Insurance (OASDI)
 - f. Other
2. Categorical
 - a. For particular occupations
 - b. For particular industries
 - c. For particular age groups
 - i. AFDC; AFDC-UP
 - ii. Supplemental Security Income (SSI)
 - d. For disabled or handicapped persons, e.g., SSI, AB, APTD
 - e. For unemployed -- unemployment insurance; GA

B. In-Kind Transfers

1. Consumption
 - a. Food: food stamps
 - b. Housing: public housing, rent supplements, house owner assistance, etc.
 - c. Clothing
 - d. Medical care: Medicaid, Medicare (as it affects poor)
2. Raising the Productivity of Low-Grade Labor
 - a. Provision of complementary facilities (roads, factories in distress areas; loans to farmers and small business), e.g., Area Redevelopment Administration (ARA)
 - b. Better job information, loans and assistance in moving
 - c. Human capital investment: increasing skills (employability) through adult education, training, retraining
3. Raising the Productivity of Future Recruits to the Labor Force
 - a. Family-planning assistance
 - b. Prenatal and postnatal care
 - c. Adding years of schooling (especially at ages 3-6), e.g., Headstart
 - d. Preventing dropouts from school

* The classification scheme presented in this exhibit is drawn from a number of sources, notably:

Fritz Machlup, "Strategies in the War on Poverty," in Poverty in America, ed. by Margaret S. Gordon (San Francisco: Chandler Publishing Co., 1965): 451-52.

Edgar K. Browning, Redistribution and the Welfare System (Washington, D.C.: American Enterprise Institute, 1975): 31.

The classifications prepared by these writers have been somewhat modified in this exhibit.

- e. Accelerating and improving school programs
 - f. Job corps for dropouts and high school graduates
 - g. Work experience for new entrants into the labor force
 - h. Work-study programs in higher education
 - i. Aid to education on all levels
- C. Composite -- Attempts to Combine Various Direct Assistance Measures in an Integrated, Composite Whole
- 1. Adding NIT, etc. to Existing System
 - 2. Integrated System of Broad-Based and In-Kind Transfers, Based on Federal Standards, e.g., Aaron's Proposal
- II. Indirect Assistance Through Subsidies or Protection to Particular Industries, Occupations, or Regions
- A. Through Price Supports
 - B. Through Limitations of Domestic Competition (entry, minimum prices, etc.)
 - C. Through Limitations of Foreign Competition (tariffs, quotas, etc.)
 - D. Through Cash Subsidies of Various Sorts
- III. Abolition of Restrictive Laws and Practices Which Purportedly Reduce Employment Opportunities (especially for low-grade labor), including the Abolition of:
- A.
 - 1. Legal minimum wages
 - 2. Trade union minimum wages
 - 3. Conventional minimum wages (employees' inhibitions)
 - B. Regressive Employment Taxes, Pension Contributions, and Other Federal Deductions from Wages
 - C. Restrictions of Access to Better Jobs (direct barriers or wage contracts limiting the amount of labor demanded)
- IV. Special Tax Advantages -- Removing All Taxes from Those Below Poverty Line
- V. Full Employment Policies: Public Employment
- VI. Increasing Aggregate Demand Through Monetary and Fiscal Expansion, especially:
- A. Increasing Government Spending
 - B. Reduced Taxes
 - D. Increased Credit Available to Business and Consumers

- breakeven income: That level of income at which the transfer is zero

These variables are mathematically related in this manner

$$\text{breakeven income} = \frac{\text{income guarantee}}{\text{marg. tax rate}}$$

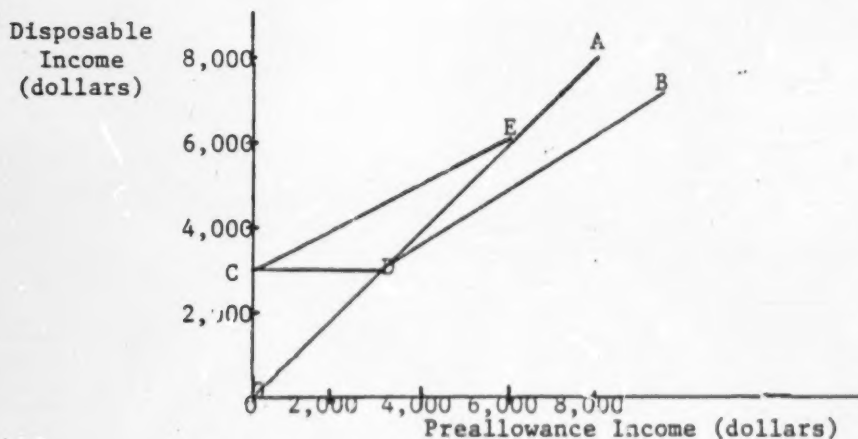
or

$$\text{breakeven income} \times \text{marginal tax rate} = \text{income guarantee}$$

Given this relationship, only two of the three variables need be specified to describe an NIT plan. For instance, an income guarantee of \$2,500 with a 50 percent marginal tax rate could be referred to simply as a \$2,500 - 50 percent NIT, which would, by definition, have a \$5,000 breakeven income.

A negative income tax can also be described graphically. Exhibit II represents the relation of preallowance income to disposable income for a family of four.

EXHIBIT II: Relation of Preallowance Income to Disposable Income for a Family of Four



OA is a forty-five degree line which represents the relation between disposable income and preallowance income if there were no income tax or transfers. OB represents this relationship with income taxes but no transfers.

For purposes of illustrating possible NIT options, the income tax will be ignored for the present. If the income guarantee is set at \$3,000 with a

100 percent marginal tax rate (i.e., dollar for dollar reductions of income transfer as earnings increase) CD states the relationship between preallowance and disposable income. For any preallowance income below \$3,000, the disposable income will always equal \$3,000. Or, to put it differently, earnings will have no consequence below \$3,000 -- the disposable income will remain the same. For a \$3,000 - 50 percent NIT, CE would represent the resulting relationship. Disposable income would increase with additional earnings, but at half the rate of the increase in earnings. A \$4.00 per hour wage, under these conditions, will have a net value of \$2.00 to the transfer recipient. Thus, there are potentially an infinite number of possible NIT alternative, with different guarantees and tax rates. Nor must a marginal tax rate be set uniformly throughout; the rate can be placed lower for lower incomes and higher for higher preallowance levels.

Compared to the present American system of welfare, a negative income tax offers several definite advantages:

1. Assistance is objectively related to need, defined as low income. Indeed, according to some writers, the NIT goes further than any other welfare design in its comprehensiveness toward eliminating poverty, insofar as poverty can be equated with low income. Since benefits vary in proportion to poverty, the NIT may, at least theoretically, represent the "ultimate weapon" in the poverty war.*
2. More assistance is given to those with lower incomes; the adjustment is automatic.
3. Since assistance is in the form of cash, the recipient is given maximum flexibility in disposing of his income.
4. The NIT is highly flexible.†

There are, however, a number of disadvantages which must be considered as well:

1. Because of the nature of the relationship between the three primary variables, any NIT design must face a problem of conflicting goals or trade-offs, with the resulting necessity for compromise. An income guarantee should be high enough to permit a "decent level of living," but the higher this figure is set, the more expensive the program becomes. A high

* Joseph A. Kershaw, Government Against Poverty (Chicago: Markham Publishing Company, 1970): 98-130.

† Edgar K. Browning, Redistribution and the Welfare System (Washington, D.C.: American Enterprises Institute, 1975): 31-64.

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marginal tax rate will offer a disincentive to work. If there is a marked decline in hours worked by the poor, the amount of transfer must increase. A low marginal tax rate, on the other hand, would extend transfers well into the nonpoor income levels. In addition to being more expensive, a low marginal tax rate would reduce the number of those who must finance an income transfer system. Regarding the breakeven income, the higher the level, the larger the income transfer necessary and the smaller the number of families above the breakeven point to support the system.

Thus, ideally, an NIT should have a low breakeven income, low marginal tax rate, and high income guarantee. These goals, however, cannot be achieved simultaneously. The necessary trade-offs involved are illustrated in Exhibit III below:

EXHIBIT III: Three NIT Programs -- Relative Advantages and Disadvantages

	<u>NIT Scheme</u>		
	1	2	3
	\$5,000 - 100% NIT	\$5,000 - 50% NIT	\$2,500 - 50% NIT
<u>Characteristics</u>	• This 100% marginal tax rate destroys all incentive to work • Cost increases as earnings decline	• higher breakeven point, \$10,000, would <u>not</u> destroy work incentive, • but would be very costly, for it would involve transfers to more than 80 million people*	• income guarantee less than poverty line, • but has work incentive features

One should carefully note that these inverse relationships between variables are not limited to the negative income tax; similar trade-offs are necessary regarding other welfare proposals, including the present system.*

2. Money does not adequately measure "need"; special circumstances, such as unusually high medical expenses, are ignored by NIT.
3. Some allege that recipients of cash transfers are likely to spend their money on nonessentials.†

* Browning, pp. 65-70.

† See Browning, p. 46

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4. The NIT treats symptoms, not causes of poverty.*
 5. There is a problem regarding frequency of payment. It is precisely low income people who need money promptly and frequently. Periodic payments will, in turn, generate numerous methodological and administrative problems, notably estimating income for the forthcoming year.+
 6. Before an NIT can be implemented, the following methodological problem areas must be addressed:
 - Definition of Income -- The use of current IRS definition of gross adjusted income would lead to grave inequities. For instance, a retired millionaire whose sole income consisted of interest from municipal bonds would be, under the IRS definition, eligible for the entire income guarantee. The definition of income under an NIT would have to be very broad.
 - Adjustment for Family Size -- Adjustments reflecting differentials under the current Orshansky measure may give an incentive to breaking up family units. A separate husband and wife with children may, together, receive a larger transfer than as a single unit. A flat per capita rate, on the other hand, would either leave a single individual with a grossly inadequate income (if the rate were low) or provide a large family with an excessive sum (if the rate were large).
 - Coordination with Federal Income Tax -- For a number of possible NIT options, a case may arise of overlap between negative tax transfer and positive tax payment. If no change is made in the tax law for this overlap group, a new high marginal tax rate would result.-

2.2.2 Wage Rate Subsidies (WRS)

Several economists** have recommended an alternate broad-based income transfer program: wage rate subsidies (WRS). The WRS subsidizes wage rates rather than annual income. The size of the transfer depends on wage rates and hours worked, not on pretransfer income. The breakeven level

* Browning, p. 34.

+ Kershaw, pp. 98-130

+ Browning, pp. 65-94.

** See Henry Aaron, Why is Welfare So Hard to Reform? (Washington, D.C.: The Brookings Institution, 1973): 60 ftn.

and rate of subsidy are the two key variables. If \$3.00 is the breakeven point and 50 percent is the subsidy rate, the subsidy for a \$2.00 market wage rate is one-half the difference between the breakeven wage rate and the market wage rate: $(\$3.00 - 2.00) 1/2 = \$.50$.

Exhibit IV presents a hypothetical WRS plan.

EXHIBIT IV: Hypothetical Wage-Rate Subsidy Plan
[\$3.00 - 50%]

MARKET WAGE RATE	SUBSIDY	NET WAGE RATE
\$1.00	\$1.00	\$2.00
1.50	.75	2.25
2.00	.50	2.50
2.50	.25	2.75
3.00	.00	3.00

Source: Browning, p.84

Advantages

In comparison to the NIT, wage rate subsidies offer a far greater incentive to work, and to work longer hours. As will be explained more fully in Section 3, work incentive effects comprise two elements. An income effect refers to the reduced need to work so hard to sustain the same standard of living resulting from increased income. A man with a minimum income guarantee of \$6,000 would, in this respect, have less incentive to work than one whose guarantee was \$2,000. A substitution effect refers to the reduced net wage rate of recipients of transfers resulting from the marginal tax rate. A man with a 50 percent marginal tax rate keeps only \$1.00 of a \$2.00 increase in wages [$\$2.00 - .50(\$2.00) = \$1.00$]. He would thus have a reduced incentive to increase his wage rate. An NIT exercises a negative incentive regarding both these factors, income effect and substitution effect. The magnitude of these negative effects would

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depend upon the income guarantee and the size of the marginal tax rate. For the WRS, however, the income effect is positive, though the substitution effect remains negative. The subsidy attached to wage rates places a premium upon numbers of hours worked -- the longer the hours, the greater the premium. But, there remains a negative incentive to increase the wage rate, as the marginal tax rate applies with increasing hourly earning rates.

One should note that higher money income does not necessarily mean that a recipient of WRS would be better off; this increase will be offset by longer working hours and reduced leisure.

Disadvantages

1. While there is a positive incentive to increase hours of work, the incentive to increase the wage rate is negative, due to the substitution effect. This will also negatively affect investment in human capital, i.e., acquiring skill through training to earn more.
2. Wage rate subsidies do not concentrate their benefits on the poor. Many nonpoor working families will receive transfers, while the nonworking poor are entirely outside the system of income transfers.
3. There are major difficulties in administration. It is necessary to know the wage rates and hours worked. This information will be difficult to acquire in the case of many occupations, e.g., waitresses, and there is great leeway for fraud.
4. There will have to be an accompanying provision for the nonworking poor, perhaps an NIT. The two programs will have to be coordinated.*

2.2.3 Demogrants ("Social Dividend Plan")

Social dividend plans, such as demogrants or family allowances, make equal cash transfers to all members of a demographic group regardless of income. In this respect, they differ from other broad-based income transfer programs [e.g., NIT, WRS] which are specifically focused on low income.⁺

* Browning, pp. 83-91.

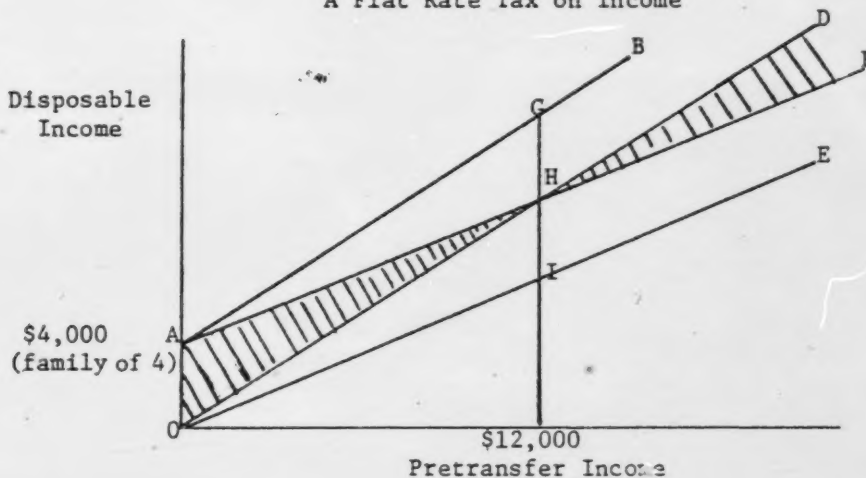
⁺ OASDI, rather than being a true insurance program, is, in fact, a broad-based social dividend income transfer plan. Economic resources are taken from the present working population to subsidize the present aged.

A demogrant is a universal social dividend, making an equal payment to every man, woman, and child in the United States. One apparent advantage of such a scheme is the fact that the same marginal tax rate would apply to everyone.

However, in practice the demogrant works out to be a modified negative income tax. If a \$1,000 demogrant were guaranteed to every American, this would require transfers to 210,000,000 people (1973), requiring \$210 billion. Edgar Browning estimates that such a sum would require an across-the-board 33 1/3 percent tax on all income with no deductions or exemptions. Assuming for the moment, a flat (proportional) tax rate of 33 1/3 percent and ignoring other government expenditures, analysis will show that this is equivalent to a \$4,000 -- 33 percent NIT. When other tax needs (e.g., defense) are included, the marginal tax rate would vary with income, with the resultant differential effects on work incentive.

Exhibit V illustrates graphically the analysis just presented.

EXHIBIT V: Hypothetical Demogrant Program Financed By A Flat Rate Tax on Income



Source: Browning, p. 82

OD represents the pretax, pretransfer relationship (1:1) between pretransfer income and disposable income. AB describes a \$4,000 demogrant for a family of four. A 33 1/3 percent income tax (flat rate) corresponds to OE. The net effect of both a demogrant and a 33 1/3 percent flat income tax is represented by AF, a \$4,000 - 33 1/3 percent NIT with a \$12,000 breakeven level income.

Once again, when nonwelfare government expenditures are included, the marginal rate will prove to be considerably higher. A \$1,000 demogrant will thus, in effect, equal a very expensive NIT with large income transfers.*

2.2.4 Family Allowances

Social dividends need not be universal, and may be established for specific demographic groups. Family allowances, one type of non-universal social dividend, award grants to families based on the number of children present. Except in the highly diluted form of tax exemptions, the United States has not relied upon family allowances for its social welfare policy, though they are common in Western Europe.†

As already noted, the number of children, not income, is the criterion for granting transfers. Most family allowance schemes classify grants as taxable income and remove income tax exemptions for children. While the wealthy can receive the benefit, many family allowance formulas specify that those above the taxpaying level should receive less than a full grant. Those in the highest bracket would find disposable income reduced.

Proponents of family allowances note that the receipt of grants would invoke no stigma and no means test. They would not impair work incentives, since additional earnings would not reduce the grant. Critics, however, note several drawbacks:

* Browning, pp. 81-83

† Daniel P. Moynihan, The Politics of A Guaranteed Income (New York: Vintage Books, 1973): 48.

- Payments must end one day, e.g., when the children become 18. Expenses must thereupon be reduced to match reduced income.
- No provision is made for the poor who are childless, e.g., aged poor.
- The payment is the same, whether to the near poor or very poor.
- Much money will go to the nonpoor.

In summary, opponents of family allowances view this policy as highly inefficient as a device to attack poverty.*

2.3 Categorical Cash Transfers

Categorical cash transfers are grants to the poor of certain demographic groups; some of the poor are singled out and others excluded. The United States has placed heavy emphasis upon this type of income transfer device in its welfare policy. Examples of categorical cash transfers include:

- Aid to Families with Dependent Children (AFDC)
- Unemployment Insurance
- Supplementary Security Income (SSI) for the aged poor, disabled, and blind
- General Assistance to Indians
- Assistance to Cuban Refugees
- Aid to Surviving Relatives of Deceased Coal Miners

Space prevents a full discussion of America's present system of categorical cash transfers. But in order to illustrate the workings of such a program, as well as to examine its advantages and disadvantages, AFDC will be singled out for analysis.

AFDC originated in the Social Security Act of 1935 as one of the public assistance programs designed eventually to be superseded by social security. In fact, AFDC has grown substantially. In addition, originally it was anticipated that a majority of recipients would be widows; by 1971, however, 76 percent of AFDC families were headed by women who were divorced, deserted, separated, never married, or otherwise living apart from their children's fathers. Ten percent of recipients were intact families, many helped under a program for unemployed fathers (AFDC-UP), first enacted in 1961. AFDC is

is a joint Federal-State program.*

Defenders of categorical cash transfers originally thought the insurance provisions of the Social Security System would eventually absorb "residual" public assistance programs. Except for old age assistance (OAA), none of these programs have declined as anticipated, and in fact have grown. This is particularly the case regarding AFDC which now surpasses all other cash transfer public assistance policies in expense and number of recipients. An argument has been made that the incidence of poverty is highly correlated with the demographic groups which are the focus of categorical programs. For instance, 54 percent of the aged have pretransfer income below the poverty line and among non-aged families headed by a female, 43 percent would be poor in the absence of transfers. Categorical grants thus are targeted to population segments with a high risk of poverty. Critics note, however, that:

- many nonpoor families are included with the poor in these demographic groups,* and
- many poor⁺ (e.g., male workers, heads of families) are excluded.

Among all the writers reviewed for this analysis, AFDC received little, if any, praise. Almost universally, it is felt that AFDC requires massive restructuring, if not complete replacement. Some of the major deficiencies of the program are the following:

1. All categorical programs require precise definitions of eligibility with some "means test" to determine whether the family meets the requisite criteria for inclusion in the program. This has often degenerated into demeaning "spot checks" and examinations to prove eligibility. Animosity between recipients and caseworkers, arbitrary judgements, deceit, and cheating are promoted under such a system.

* Aaron, pp. 7-11.

+ Browning, pp. 35-36

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2. In origin, many of these categorical programs were based on the distinction between "deserving" and "undeserving" poor. In fact, however, there is no way to rationally make this distinction. There are too many factors which enter into a family head's decision whether to work, and these factors interact in a very complex manner. Furthermore, among fatherless families with preschool children, about one-half of the mothers work; more than 40 percent of women now (1973) receiving AFDC worked at least part of the year. Regarding unemployment insurance, 83 percent of recipients were from families making more than \$5,000 a year (1973).*
 3. Levels of benefits and numbers of eligible vary widely among the fifty states; AFDC, in practice, therefore is capricious.

Under the joint Federal-State program, states have adopted such diverse benefit levels and administrative rules that fifty-one separate public assistance programs are in operation in the fifty states and the District of Columbia. Annual average payments to a family of four can vary from \$670 in Mississippi to \$3,730 in New York (1971).

These variations arise from a number of sources:

- States set different standards of need (full standards).
 - Not all states pay recipients the full standard (maximum payment).
 - States pay for certain work-related expenses, but each defines them differently.
- f. AFDC has a high marginal tax rate with the consequent negative work incentive. Prior to 1967, this rate was 100 percent -- \$1.00 was subtracted from the transfer for each \$1.00 of earnings. Since then, the benefits have fallen 67 percent for each dollar of earnings beyond the first \$30.00 each month.⁺
 5. Recent studies** have suggested that AFDC may contribute to the breakup of families. "The data imply. . .that independent of other factors, the size of the AFDC payment⁺ itself was an important determinant of family dissolution.⁺⁺

* Browning, pp. 36-39.

+ Aaron, pp. 7-11.

+ Browning, p. 38.

** U.S. Congress, Joint Economic Committee, Subcommittee on Fiscal Policy, Studies on Public Welfare, Paper No. 12, Part I, 93rd Congress, 1st Session, November 1973. Study on "The Impact of Welfare Payment Levels on Family Stability," by Marjorie Honig, pp. 51, 38.

++ Browning, pp. 38-39.

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In summarizing his conclusions regarding categorical cash transfer programs, Edgar K. Browning stated:

Categorical programs are essentially NIT programs restricted to certain demographic groups. They have all the disadvantages of the NIT, together with several additional ones, but lack most of the advantages.*

2.4 In-Kind (Consumption) Transfers

In-kind transfers assist the poor by financing consumption of particular goods and services. Examples of such programs include food stamps, housing subsidies, and Medicaid. Food stamps will be looked at closely here.

2.4.1 Food Stamps

Eligibility for food stamps depends upon family size and income. A family of four is eligible if its income is below \$6,800, after deductions for such items as housing and utility costs in excess of 30 percent of income. Once eligible, a family can purchase food stamps at a price below their face or market value.

The amount of the discount comprises the value of the food stamps, and will vary with income and family size, as displayed in Exhibit VI. Thus a family of four which has a gross adjusted income of \$3,000, can purchase \$1,800 worth of food stamps for \$852. In effect, the government will pay for 53 percent of its food bill.

* Browning, pp. 38-39.

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EXHIBIT VI: Food Stamp Benefits for a Family of
Four (July 1974)

Pretransfer Adjusted Income	Transfer	Total Adjustment	Minimum Food Consumed
0	1,800	1,800	1,800
1,000	1,572	2,572	1,800
2,000	1,308	3,308	1,800
3,000	948	3,948	1,800
4,000	660	4,660	1,800
5,000	444	5,444	1,800
6,000	288	6,288	1,800

Source: Browning, p. 41.

While there is a variable purchase option, most recipients elect to purchase the basic \$1,800 allotment. The effect is to place an \$1,800 floor on food purchases. There is an implicit marginal tax rate of approximately 25 - 30 percent.

One noteworthy feature of the food stamp program is its effect upon consumption patterns. Some economists argue that in-kind transfers distort consumption patterns, forcing a recipient to purchase more of a particular commodity than would have been the case if the transfer had been unrestricted. One scholar estimates that \$1.00 in food stamps is worth \$.82 to the recipient.*

2.4.2 Evaluation of In-Kind Transfers

The usual argument made in favor of in-kind transfers as social policy is that they promote the consumption of essential items (housing, medical care, food), and discourage frivolous purchases (e.g., excessive tobacco, movies, liquor). Opponents, however, note that:

* Kenneth Clarkson. See Browning, pp. 40-43.

1. The assumption is often made that experts would be able to evaluate each family's needs and make sure that the appropriate quantity and quality of goods are consumed. The reality, however, is far different. Existing in-kind transfer programs are adjusted for only a few variables, e.g., income and family size. All kinds of variables are ignored in order to make these programs administratively manageable.
2. Evidence does seem to indicate that the poor do consume more now than before food stamps. This does not necessarily imply more nutritious diets, however.
3. To fine-tune allotments would require far more information than presently available. There is a question whether such an elaborate information system would be administratively manageable.
4. Consumption survey data seem to indicate that the poor actually spend proportionately more on food, housing, and medical care than higher income groups. Evidence of widespread irrational purchases is lacking.
5. Administrative costs are often quite high for in-kind transfer programs in comparison to simple cash transfers. At least 9 percent of the amount transferred under food stamps is allocated for administrative expenses, compared to the approximately 2 percent for social security. A full-scale NIT, it is estimated, would involve an overhead of around 3 percent.
6. Like categorical cash transfers, in-kind transfers are truncated NIT programs, often with severe disadvantages lacking in a full-scale NIT.*

2.5 Composite Programs

Of course, there are also proposals to build upon the existing array of programs (cash transfers, in-kind transfers) and merge them into an integrated, reformed system. Any consideration of welfare reform, and particularly of proposals to "fine-tune" the present system must examine the totality of some 168 existing programs: their discrete effects and interactions. Exhibit I on page 3 illustrates, to some degree, the complexity of such an undertaking.

* Browning, pp. 45-50.

More than simple direct transfers of income are involved.

Some analysts do not think an attempt to integrate existing programs to be worth the effort:

- Contradictions and anomalies pervade the present welfare system. Defects of individual programs are often magnified in combination. For instance, an across-the-board increase in social security will result in no improvement for the elderly poor who are presently receiving SSI as well as social security. Higher social security payments reduce SSI payments, dollar for dollar.
- The combined effects of programs often destroy all work incentives. The effective marginal tax rates of several programs is approximately the sum of the separate rates. Rates can exceed 100 percent on some income levels.*
- A system, which consists of 168 discrete programs, administered on several levels of government, will interact with such incredible complexity, that their net effects will often be hard to determine.†

An interesting alternative composite approach is suggested by Henry Aaron.‡ He recommends a tripartite composite made up of cash allotments, housing subsidies, and medical care. If cash, housing, and medical assistance were provided using the formulas he developed, and if the tax rate were imposed sequentially, the basic benefit for a family of four with no outside earnings would be worth \$3,410. Benefits in the form of cash would be available until earnings reached \$7,728. Aaron avoids the horrendous cumulative tax rates which either presently exist or would arise in combination with proposed welfare reforms (e.g., FAP). These rates are still high, however, approaching 80 percent at some income levels. On the whole, Aaron's system, if adopted, would result in a vastly improved equity and would improve work incentives.

* Aaron, pp. 31-46

† Browning, pp. 59-63.

‡ Aaron, pp. 59-69.

3.0 WELFARE REFORM: MAJOR ISSUE AREAS

3.1 Summary of Issue Areas

Exhibit VII presents a detailed abstract of issues raised by the welfare reform controversy, grouped into five interrelated issue clusters:

- normative issues
- economic issues
- social issues
- administrative issues
- political issues

A full discussion of all these topics is impossible in a report of this size. However, one issue has stood out as of paramount significance among writers on the subject of welfare reform: the question of work incentives and their importance. This section will, therefore, focus on the matter in detail, assessing its relevance in the redesign of America's public assistance system. Specifically, the following questions will be addressed:

- Of what economic importance are work incentives?
- What effect does the marginal tax rate have on work incentives? Is there empirical evidence to document these effects?
- For the nation as a whole, what is the overall effect of redistribution of income upon the marginal tax rate?

3.2 Of What Economic Importance Are Work Incentives?

Work incentives are important because they affect the cost of a program of public assistance, the available tax base to support such a system, as well as long-term economic growth. Two factors actually comprise work incentive effects:

- income effect -- increased aggregate income reduces the need to work as hard to sustain a comparable standard of living.
- substitution effect -- higher marginal tax rates reduce the net wage rate of recipients of transfers as earnings increase. The marginal tax rate is the proportion of reduction in transfer payments as earned income rises.

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EXHIBIT VII: Issue Area Abstract

I. Normative Issue Cluster

A. Equality

1. To what extent is equality, however defined, a desirable social goal?
 - a. In addition to income equality, what varieties of equality are there?
 - b. Do various forms of inequality serve a social good?
 - c. Should income equality be considered synonymous with equality? Should it be considered the criterion of human happiness?
2. Can income equality, in fact, be measured?

B. Need

1. Welfare programs concentrate on economic need. Are other needs important? Can government social programs address these other needs?
2. If the goal of a welfare program (i.e., income redistribution) is to provide economic resources proportionate to need, to what extent do present or proposed measures achieve this?
 - a. Adequacy -- Is the minimum income guarantee adequate for subsistence? For socially defined "decency"?
 - b. Coverage -- Are all the poor, once identified, in fact covered by welfare programs? Are resources distributed proportionate to need?
3. Objectivity -- Are income transfers objectively (empirically, quantitatively, and clearly) related to need? To what extent do present and proposed programs demonstrate a clear linkage?
4. "Deserving" vs. "Non-Deserving" Need -- To what extent can "deserving" and "non-deserving" groups of the poor be distinguished? What are the criteria of "deserving"? Can the "deserving" poor, however defined, be reliably delineated in practice?

II. Economic Issue Cluster

A. Conceptual Economic Issues in Design of Welfare Programs

1. Of what importance are work incentives? How do they affect overall economic growth? Individual productivity? Cost of income transfer programs? What are the relative effects of the work incentives components: income effects and substitution effects?
2. What effect does the marginal tax rate have on work incentives?
 - a. What is the effect of marginal tax rates on earnings?
 - b. On investments in human capital?
 - c. What are the marginal tax rates of present programs considered discretely? Considered cumulatively?
 - d. How do proposals for reform handle marginal tax rates?

- e. What empirical evidence exists regarding the precise work incentive effects of income maintenance programs?
 3. Cost of Redistribution -- What is the overall effect of national redistribution of income upon the marginal tax rate? How much can society afford by way of increased marginal tax rates to support income transfers? Given this limit, what income guarantees and breakeven levels are possible?
 4. How are the "poor" defined?
 5. What is the current state of income redistribution?
 - a. How many are poor?
 - b. How much transfer of income already is channeled to the poor?
 - c. What is the distribution of income?
 - d. What are the current consumption patterns of the poor?
 6. Flexibility -- To what degree do various income maintenance proposals display flexibility; that is, the capability to be modified to meet newly perceived needs?
 7. Economic Value -- To what extent does the face value of a transfer correspond to the value placed on it by a recipient?
 - a. Is there a gap between cost to society and value placed by recipients?
 - b. Are there distortions in consumption patterns? Do consumers spend transfer income in ways different from ways they would spend it free of restrictions?
- B. Methodological Issues in Implementation of Welfare Reform
1. Income -- How is pre-allowance income defined? Is the IRS classification of "gross adjusted income" sufficient? If not, what should "income" encompass?
 2. Treatment of Family Unit -- In addition to pretransfer income, an income transfer program must account for differences in family size. What are the available means for doing so? What are the relative advantages and disadvantages of these options:
 - approximately the same proration according to family size used in the present official poverty measure,
 - equal per capita guarantee,
 - per capita guarantee of \$1,200 for each adult and \$800 per child?
 3. Coordination with Federal Individual Income Tax -- There will be a problem in coordinating a program of income guarantees (e.g., NIT) with the positive income tax, if the breakeven income of an NIT exceeds the sum of exemptions and deductions under the Federal income tax. How can this "overlap" be handled without creating very high marginal tax rates and inequities?

III. Social Issue Cluster

- A. Externalities -- Some proponents of in-kind transfers take the position that externalities (economic and social benefits to others flowing from transfers to the poor) arise from these programs. To what extent does the empirical evidence support this supposition?

- B. Stability of Family Unit -- Critics of existing categorical cash transfers (e.g., AFDC) maintain that these programs often promote the disruption of family units. Have empirical studies shown this to be the case? Do proposed reforms promise to remove incentives to break up family units?

IV. Administrative Issue Clusters

- A. Coordination and Control -- The large number of existing social assistance programs and the complexity of jurisdictional divisions between Federal, state, and local government create grave difficulties regarding coordination and control. What are the consequences of lack of sufficient control? How have present programs failed in this regard? Do welfare reform proposals give attention to this issue? If so, how?
- B. Administrative Costs -- What are the administrative overheads associated with different welfare reform models? Which have the lowest?
- C. Eligibility -- How will eligibility for a given welfare program be determined?
- D. Filing and Payment -- How frequently will payments be made? Under an NIT, the program does not immediately fill the income needs of an individual suffering a sudden loss of income. Can a system be designed for frequent, periodic payments?
- E. Audit Standards -- Direct assistance programs will require a determination of pretransfer income. What kinds of audit procedures are available to assure accuracy and avoid fraud? Can sampling procedures maintain credibility of enforcement? Would IRS be the best agency for regular auditing procedures?
- B. Jurisdiction in Administration -- Which Federal agency should have primary responsibility in the implementation of a major welfare reform system? DHEW? IRS? What role can CSA play as an advocate of the poor in this process?

V. Political Issues

- A. Interest Groups -- What are the different constituencies affected by the welfare system (e.g., trade unions, activist spokesmen for minority groups, politicians)? What has been their behavior in the past with respect to different welfare proposals? What is their current position? How would they likely react to initiatives in this area by the Carter administration? What would be the likely impact?
- B. Congress -- What is the current attitude of Congress? What versions of welfare reform are supported there? By whom? What do committee staffers think?

- C. Research Institutes -- What is the current role of research institutes ("think tanks"), such as Brookings, in this affair? What has been their involvement in the past? What role do they seek for themselves now?
- D. Executive Branch -- What position does the Carter administration take regarding welfare reform issues and alternative proposals? In what way can CSA contribute to a meaningful discussion of welfare issues as the new administration assesses its options?

Any income guarantee linked to earnings will have a negative income effect by eliminating the necessity to work for that amount. The higher the income guarantee, the greater the negative income effect. However, an income transfer program linked to wage rates and hours worked, such as WRS, will have a positive income effect by increasing the economic value of hours worked.

Since all transfer programs prescribe some reduction in payments proportional to earnings, they will exercise a negative substitution effect. The loss in transfer reduces the net value of new wage earnings received. For instance, with a 50 percent marginal tax rate on transfers, a worker who increases his earnings by \$1.00 per hour will have a net increase in disposable income of only \$.50. This, naturally, will diminish the incentive to increase one's wage rate and annual earnings.

A reduction in the hours worked by recipients of income transfers concerns economists because of cost implications for a welfare design:

1. Each percentage point decline in earnings will result in a corresponding increase in transfer payments of approximately 1 percent.
2. The larger the disincentive effect, the more difficult and expensive it will be to increase the disposable income of the poor.
3. High disincentive features may influence those just above the transfer eligibility line to reduce work effort as well. This will increase the number of recipients, the cost of the program, and will, incidentally, also reduce the available tax base to support the program.
4. Many believe, on philosophical grounds, that work is necessary to give meaning to life and promote a sense of personal worth. Policies tending to create a "dole" may be destructive to self-respect and human dignity.*

* Browning, pp. 69-73.

3.3 What Effect Does the Marginal Tax Rate Have on Work Incentives? Is There Empirical Evidence to Document these Effects?

3.3.1 The Importance of the Marginal Tax Rate

Marginal tax rates with their attendant substitution effects are believed by most economists to be of crucial importance in evaluating welfare reform proposals. High marginal rates potentially can:

- reduce work effort of both taxpayers and recipients,
- reduce the incentives to save and invest, including investments in human capital,
- create an incentive to convert income into nontaxable form, and
- by reducing overall productivity, can endanger long-term economic growth.*

Consider the question of incentives to invest in human capital. This refers to the willingness of workers to undergo training or any educational program resulting in increased earning capacity. If a \$3,000 - 50 percent NIT were in effect, a man with an annual income of \$4,000 would receive \$1,000 in transfer payments. Supposing he could increase his earnings to \$6,000 per year by undergoing training, the actual increment of increased disposable income would not be \$2,000, but \$1,000 [\$2,000 - \$1,000 lost transfer]. The 50 percent marginal tax rate will thus impair the incentive to improve one's marketable skills. As Browning noted:

In the short run, work incentives may be impaired by a high marginal tax rate and, in the long run, work skills may be allowed to deteriorate or may never be acquired in the first place. . . .

* Browning, p. 100.

+ Ibid., p. 75.

3.3.2 Empirical Evidence Concerning Marginal Tax Rates and Their Effects

3.3.2.1 Marginal Tax Rates of Existing or Proposed Programs

While it is often very difficult to assess the net effect of America's present morass of 168 programs,* evidence that does exist suggests that the effective marginal tax rates are quite high. This is particularly true for the cumulative effects of several programs examined together: marginal rates are often additive. Henry Aaron did extensive research on the subject and concluded that the tax rates for a family of four under AFDC in combination with in-kind benefits average 75-80 percent for most low earnings levels. In addition, there is the notorious "notch" effect whereby a person can receive less disposable income by earning more. This can occur around the upper income limits of eligibility.

Perhaps more interestingly, Aaron calculated the net tax transfer rates which would have arisen under various legislative proposals for reform: Nixon's original FAP, HR 1, and the Long Plan. Their cumulative rates were considerably higher than under the present system, and would have affected far more families than the present AFDC. For some earnings levels, HR 1 would have resulted in marginal tax rates of 130 percent.⁺ Some economists, therefore, argue that an NII or other significant welfare reform must not be merely added to the existing system, but must replace it.⁺

3.3.2.2 Effects of Marginal Tax Rates

Economists agree that high marginal tax rates have a negative work incentive effect; the exact quantitative measure of this effect is, however, open to dispute. This section will review the evidence available

* Browning, p. 63

+ Aaron, pp. 31-46.

+ Browning, p. 91-94.

on this question, with special emphasis on present government-sponsored income maintenance experiments.

1. Nonexperimental Evidence

Irwin Garfinkel* found disagreement among various studies regarding the extent of work reduction caused by potential income maintenance programs. The estimated reduction in work effort for prime-aged married men under a \$3,000 - 50 percent NIT (family of four) ranged from 3 percent to 40 percent.⁺ Clearly, there was a wide range of uncertainty.⁺

2. Income Maintenance Experiments

Four major experiments in negative taxation have been sponsored by the government. Originally developed under the auspices of the Office of Economic Opportunity (OEO), the Department of Health, Education and Welfare now exercises supervision. The Institute for Research on Poverty of the University of Wisconsin and Mathematica, Inc. of Princeton, New Jersey have played leading roles in their implementation. The four experiments included:

- The New Jersey - Pennsylvania Graduated Work Incentive Experiment (1968-1972)
- The Iowa - North Carolina Rural Income Maintenance Experiment
- The Seattle Experiment
- The Gary, Indiana Experiment

The results of the first two of these experiments will be reviewed here.

The New Jersey Graduated Work Incentive Experiment⁺

The experiment examined eight combinations of income guarantees and tax rates as to their relative effects upon a sample drawn from the poor and near poor (125 percent or less of the poverty line). They were matched to a control group. The study concentrated on male-headed urban families, and lasted three years.

* U.S. Congress, Joint Economic Committee, Subcommittee on Fiscal Policy, Studies in Public Welfare, Paper No. 13, 93rd Congress, 2nd Session, February 1974, pp. 1-32.

+ Browning, p. 71.

⁺ Harold W. Watts and Albert Rees (eds.), Final Report of the New Jersey Graduated Work Incentives Experiment, Vols. 1, 2, 3 and David N. Kershaw and Jerilyn Fair (eds.), Vol. 4 (University of Wisconsin-Madison, Institute for Research on Poverty, and Mathematica, 1973, 1974).

Also see: Joseph A. Pechman and P. Michael Timpane (eds.) Work Incentives and Income Guarantees: The New Jersey NIT Experiment (Washington, D.C.: The Brookings Institution, 1975).

The major finding of the experiment was that there was only a small (5 to 6 percent) reduction in average hours worked by the male heads of recipient families. For working wives, the reduction was greater: about one-third of the previous work effort for whites and more than one-half for Spanish-speaking wives. Black working wives were not affected.

There were, however, a number of severe methodological difficulties which render these results inconclusive:

- The limited time period of the experiment made it more difficult to assess the impact of a permanent, national NIT.
- There was a major change in the New Jersey welfare system during the course of the experiment which may have contaminated the results. One reason for selecting New Jersey in the first place was the lack of an AFDC-UP program for unemployed fathers. But on January 1, 1969, the state adopted such a program, with very generous provisions. As a result, controls became subject to income maintenance policies often more generous than the experimental NIT groups. Furthermore, there was large scale attrition in the experimental samples, notably among the less generous NIT groups.
- Only a small fraction of those who would be covered by a national program were included in the experiment. A national program may have different labor market effects than a local experimental program -- e.g., reduction in normal work week for low-skill laborers to thirty hours.*

The Iowa - North Carolina Rural Income Maintenance Experiment

The New Jersey experiment focused on the urban poor, and the results cannot necessarily be generalized to the poor of rural areas. The Iowa - North Carolina NIT experiment was designed to fill this gap. Families meeting income criteria were randomly selected and placed in five different experimental treatment groups. Benefit levels ranged from 50-100 percent of the poverty level income and implicit tax rates from 30 to 70 percent. Both wage-earning and self-employed workers were studied.

For wage earners, hours worked for wages were lower among experimental group members compared to controls by a weighted average of 13 percent after

* Pechman and Timpane, pp. 7-14.

holding constant nonexperimental differences. Hours worked by men remained essentially unchanged, but for wives, a negative experimental effect of 27 percent was observed.

Among experimental farm operators and managers, declines in farm profits appeared, relative to controls, but the differentials were only marginally significant. Concerning hours worked, a curious anomaly was observed. Farm work by farm operators showed a positive experimental effect of 11 percent in both states. Farm hours declined over time for all groups, but at a faster rate for controls than for experimentals. Experimental wives also seemed to work longer hours than controls. Implicit tax rates and benefit levels appeared to have no effect on level of farm work. Thus, a decline in productivity was evident, despite more hours worked among farm operators compared to controls.*

Conclusions

The available evidence seems to suggest that economists' concern about work incentives is not misplaced, but that fears of a complete cessation of work are unjustified.†

3.4 What is the Overall Effect of National Income Redistribution Policies Upon the Marginal Tax Rate?

One major segment of the work incentive question concerns the cost of redistribution: What are the costs of income redistribution for society as a whole, both in terms of net transfers, and in marginal tax rates which taxpayers must bear? Usually the cost of redistribution is defined as the net amount of redistribution which a given plan would accomplish. Thus, it

* DHEW, Summary Report: Rural Income Maintenance Experiment (Washington, D.C.: DHEW, 1976): vi-xviii.

† Browning, p. 73.

was estimated that a hypothetical \$4,000 - 50 percent NIT would yield a net transfer (redistribution cost) of \$27.5 billion in 1971. A \$5,500 - 50 percent NIT* would have, according to some, cost \$71 billion in the same year. Sometimes, these costs were represented as percentages of the GNP: respectively, 2.5 percent and 6.5 percent for the two plans.

There are economists who maintain that this grossly underestimates the true cost of redistribution. Edgar Browning, for instance, has emphasized that marginal tax rates, not percent of GNP, are the key variable in assessing cost to society. He estimated that a \$5,500 - 50 percent NIT in 1971 would have resulted in an 80 percent marginal tax rate for all families in the United States. A rate of this magnitude he felt to be ruinous.

To illustrate why this was so, Browning constructed a hypothetical model of a demogrant with an income guarantee set at one-half the average (not median) family income. In 1973, this amounted to a \$6,750 ($\$13,500/2$) income guarantee. For purposes of simplicity, he assumed three premises in his analysis:

- the demogrant program was the only government expenditure,
- demogrant would be financed by a proportional (flat rate) tax on pretransfer income, and
- all families were of equal size.

Two of these premises were dropped later in his analysis. Browning stated that a demogrant of this type would be equivalent to a \$6,570 - 50 percent NIT with a breakeven point equal to the mean family income (\$13,500). In effect, the upper half of the income curve would redistribute economic resources to the lower half. Browning estimated that this plan would result, given America's present distribution of income, in a net transfer of 10 percent of the

* recommended by the NWRO.

national income. From this, he concluded further that for each one percent of total income redistributed, the marginal tax rate must be increased by 5 percent for the entire population.*

While there is disagreement as to the upper limit of marginal tax rates before serious work disincentives arise, Browning assumes 50 percent to be the maximum safe limit. Subsequently, Browning factored in other government expenditures and the taxes needed to finance them, which amounted to around 22 percent of the Net National Product in 1973. Thus, he concluded that 28 percent is the actual upper limit of income transfer marginal tax rates (50 percent - 22 percent = 28 percent). Given this limit, 28 percent of \$13,500 is \$3,750, the highest safe minimum income guarantee, according to Browning.

But the real marginal tax rates of many plans are significantly higher than that. The NWRO \$5,500 - 50 percent NIT, according to Browning, would have resulted in a marginal tax rate close to 80 percent for the entire population.

Browning feels that the real significance of this fact is that the marginal tax rate would apply to the middle and upper income class. Since these groups generate the bulk of economic resources in the country, a severe work disincentive affecting them would seriously erode the tax base and compromise future economic growth.+

Regardless of the validity of Browning's specific conclusions, it seems clear that serious consideration must be given to the overall impact of different welfare reform strategies upon the marginal tax rates (and consequent work incentives) for the nonpoor as well as for the poor.

* To redistribute 10 percent of income required a 50 percent marginal tax rate. Thus the 1:5 proportion.

+ Browning, pp. 96-111.

4.0 CSA'S POTENTIAL ROLE IN WELFARE REFORM

4.1 The Unfolding Scenario

In the preceding pages, we have presented a brief overview of the range of issues and topics likely to be considered by the DHEW review. When particular topics emerge in the coming months, we will be able to provide more focused analyses.

Of particular concern to CSA at the present juncture, however, ought to be three sets of questions:

- How will the agency relate to DHEW as that department moves forward with its review? Secretary Califano has said that his review will involve all Federal agencies that have an interest in welfare reform, as well as state and local governments and interests. But, just how will CSA relate to the review process, structurally?
- How will CSA relate to the welfare reform review, substantively? Which of the topics outlined in preceding pages of this report are most appropriately of concern to CSA?
- Where governmental reorganization occurs (as it most surely will) following a Federal welfare reform initiative, what might CSA's new role be? Closely related, where is CSA likely to land as a result of such reorganization?

Each of these questions will be considered below. No conclusions will be reached. However, the options that appear to be likely candidates for consideration will be presented, with no attempt to evaluate their merits. That evaluation must come later, as events unfold, and as CSA begins to shape its policy perspectives vis á vis welfare reform.

4.2 CSA's Possible Roles in Welfare Reform: Some Likely Options

4.2.1 Structural Options: Relationships to the DHEW Review

There are (at least) four possible ways CSA might relate to DHEW's welfare reform review (these are not mutually exclusive options):

- a. No formal relationship -- If DHEW makes no overtures to CSA and CSA, in turn, makes no overtures to DHEW, it is quite possible that CSA could be "left out" of the review process.

- b. Occasional informal contact; some review and comment -- This option is also possible. However, it might not be consistent with Secretary Califano's expressed intention to solicit broad participation from the Federal "family."
- c. Occasional formal contact; review and comment through some kind of advisory committee mechanism -- Certainly this is a likely vehicle. The secretary might even utilize the Inter-agency Poverty Studies Task Force. Whatever vehicle might be chosen, CSA would want to be a formal participant.
- d. A formally defined role; possibly, involving the CDC/CAA network -- CSA is the only Federal agency with an ongoing, active grassroots constituency comprised of representatives of low income communities. As the welfare reform review and subsequent initiative evolves, this "outreach/constituency" network could be envisioned as playing an important role, both in shaping options and in facilitating program implementation. Alternatively, one wonders about the costs to the White House, DHEW, etc. of not involving grassroots constituencies of the poor early in the process. This option may be CSA's best "shot" at a prominent and enduring role in the welfare reform initiative.

4.2.2 Substantive Options: Relationships to the DHEW Review

Realistically, CSA must recognize the critical mass of analytical work already in place for the welfare reform review, as well as the large number of skilled analysts in place at DHEW (i.e., ASPE -- Income Security Group). However, one observation can be made (based on our experience with DHEW's Office of the Secretary):

The analysis process might well be excessively arcane and scholastic, lacking in understanding of practical realities of low income communities, and also building conclusions on highly tenuous data bases.

In this context, the potentialities of the Market Baskets Study should not be overlooked. However, in "publicizing" the Market Baskets Study, CSA should not oversell it, especially in view of the time constraints. But, there might be an opportunity -- over the next few months -- to weave into DHEW's review, a sensitization to the issues being confronted in the Market Basket Study.

In essence, then, three possible substantive options (among others) emerge in the short run:

- a. Articulation of the kinds of information the Market Baskets Study might provide and how such information would sharpen the welfare reform process — Most writers who discuss welfare strategies assume, as given, two vital premises:

- poverty has been validly defined such that the poor can be reliably delineated, and
- rationally constructed "poverty lines," in fact, have been established which are truly representative of a minimally decent standard of living.

Usually, the Orshansky measure is uncritically accepted as appropriate for this purpose.

Currently, poverty measures or income eligibility standards are extensively used by a variety of Federal agencies in the administration of national programs designed to help the poor. These measures have had two primary uses:

1. An allocative formula to distribute appropriations among states and other jurisdictions [e.g., Title I of the Elementary and Secondary Education Act].
2. Income eligibility criteria for individual applicants [e.g., CSA administered programs].

There is, however, considerable diversity regarding which specific measures to apply. While the official Orshansky Measure is widely utilized, other formulas are also used, and in addition, the official measure is often modified or simplified, reducing the number of thresholds. Income definitions also vary.*

Furthermore, there is general agreement by specialists dealing with this question⁺ that the current Orshansky poverty thresholds are in need of major revision or replacement. Major welfare reform innovations will not end the need for such measures; on the contrary, scientifically based thresholds founded on absolute standards of need will become all the more necessary in order to rationally distribute Federal monies. Whatever income maintenance formula is adopted, there must be some rationale for drawing a "break point" between net receipt of support and payment of taxes. The amount of support will also have to vary with income in such a way as not to penalize productive work.

* DHEW Poverty Studies Task Force. The Measure of Poverty, pp. 14-17.

⁺ See TARP Institute, The Development of Low Income Market Baskets: A Work Plan (Washington, D.C.: TARP Institute, 1976): 20-22.

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Absolute poverty measures, as envisioned in the Market Baskets Study, can fill this need. This project is designed to achieve greater conceptual and methodological clarity in the establishment of critical market baskets, based on absolute measures of need. Once constructed, these market baskets can be linked and costed out to provide "poverty thresholds" of a minimally acceptable standard of living (whether defined as subsistence or adequacy). Currently, however, a great deal of conceptual and empirical work must be completed before low income market baskets of consumption goods and services can achieve their potential.

The completion of these research and development activities will result in the development of poverty thresholds which will, in fact, have a scientific basis, insofar as the current state-of-the-art permits. Policymakers, in considering alternative welfare reform proposals, will thus be able --

- to propose "break points" based on a plausible rationale,
- to price out their likely costs,
- to identify the administrative and fiscal implications of different proposals.
- to pinpoint the relative impact of different proposals on different population segments of the poor, and
- to evaluate the true impact of Federal poverty programs.

In conclusion, it seems clear that the Market Basket Study will prove very useful to those Federal policymakers considering different income maintenance designs. This fact is CSA's major strength in the forthcoming welfare reform discussions and ought to be emphasized.

- b. Critical analysis of substantive economic proposals; e.g., the real world implications of establishing a guaranteed income minimum at a particular level-- CSA could (at least potentially) provide a reality test in the form of first-hand knowledge of the experiences of low income families and communities.
- c. Critical analysis of various options for reorganizing the administration of categorical assistance programs -- The focus of such critiques could be on the impacts of alternative arrangements on the organization of local programs, hardships caused by shifts in eligibility criteria, etc.

4.2.3 Administrative Options: CSA's Location in the Federal Bureaucracy

CSA's role in any reformed and reorganized system of public welfare will, to a very great extent, depend on (1) how the agency is organ-

ized; (b) its location within the Federal bureaucracy; and (c) functions assigned to it.

Among the locational options available:

- a. No change -- It is quite possible that CSA could remain an independent agency. This might be considered desirable because of its unique advocacy function.
- b. Become part of HEW or HUD -- Certainly this is an option that will be considered -- primarily because CDC/CAA service functions overlap categorical service programs currently funded through these agencies.
- c. Become affiliated with a new agency; for example, a newly-formed consumer protection agency -- This option should be considered; although, CSA's service functions do not, prima facie, appear compatible with the ombudsman-regulatory missions slated for a consumer protection agency. However, if CSA were to no longer be a service agency, it is conceivable that an ombudsman/advocacy mission, particularly suitable to the consumers movement, could gain ascendancy.

5.0 WELFARE REFORM: A SELECTIVE BIBLIOGRAPHY

Among the hundreds of possible citations, TARP has chosen the following highly selective list of books, monographs, and articles which treat the subject of welfare reform. For those interested in pursuing the subject beyond the brief overview presented in this report, TARP recommends first reading the citations with an asterisk.

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